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**SF 512** – Water Quality (LSB1844SZ)

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Fiscal Note Version – New (successor to SF 482)

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**Description**

**Senate File 512** exempts the sale of water by utilities from the State sales tax and creates a Water Service Excise Tax on metered water that is deposited in the General Fund. These funds are then transferred incrementally as follows:

- FY 2019: a total of one-sixth of the tax will be transferred from the General Fund, with half of the funding distributed to the Water Quality Infrastructure Fund and half to the Water Quality Financial Assistance Fund.
- FY 2020: a total of one-third of the tax will be transferred from the General Fund, with half of the funding distributed to the Water Quality Infrastructure Fund and half to the Water Quality Financial Assistance Fund.
- FY 2021: a total of one-half of the tax will be transferred from the General Fund to the Water Quality Financial Assistance Fund. This will happen each fiscal year through FY 2030.
- The tax is repealed on July 1, 2029, or if the State sales tax is increased.

**Water Quality Infrastructure Fund.** For FY 2019 through FY 2020, funding will be allocated from the Water Service Excise Tax to the Fund as stated above. Beginning in FY 2021, the Water Quality Infrastructure Fund will be appropriated \$15.0 million per year from wagering tax receipts that are currently paying off Vision Iowa Bonds. The Division of Soil Conservation and Water Quality of the Department of Agriculture and Land Stewardship (DALs) will administer the Fund and can use up to 4.0% of the Fund for administration. The Fund is repealed after all moneys have been expended.

The Fund will support two types of projects as detailed in the [Iowa Nutrient Reduction Strategy](#):

- The Edge-of-Field Infrastructure Program supports projects to capture or filter nutrients that can enter surface water. These are long-term projects that include wetlands, bioreactor systems, saturated buffers, and land use changes.
- The In-Field Infrastructure Program supports projects to decrease erosion and surface water runoff. These are long-term projects that include terraces, waterways located on cropland, soil erosion control structures, and managed drainage systems.
- The Division can support multiple projects at one location and can combine projects from both Programs.
- To measure the progress toward meeting Iowa Nutrient Reduction Strategy goals, the baseline is calculated for the time period from 1980 to 1995, the same time period used in the federal Environmental Protection Agency (EPA) Gulf Hypoxia Action Plan. Refer to the Mississippi River/Gulf of Mexico Watershed Nutrient Task Force [2015 Report to Congress](#) for additional information.

**Water Quality Financial Assistance Fund.** Creates the Water Quality Financial Assistance Fund in the State Treasury and appropriates moneys from the Water Service Excise Tax to the Fund. For FY 2019 through FY 2030, funds will be appropriated annually as follows:

- 40.0% to the Iowa Finance Authority (IFA) for the Wastewater and Drinking Water Financial Assistance Program. The IFA will administer the Program that consists of appropriations, interest, and other funds. The Program will be expanded to include “drinking water” and source water protection projects. The IFA can use 1.0% of the funds for administration. The IFA is required to submit an annual report to the Governor and the General Assembly beginning October 1, 2018, detailing the expenditures of the previous year. The Program is amended to give priority to communities that employ technology to address the latest version of the Nutrient Reduction Strategy. Eligibility is expanded to include utility management organizations and rural water systems.
- 45.0% to the IFA for the Water Quality Financing Program that funds projects to improve the quality of surface water and groundwater. This is a loan program, and the IFA will set the loan interest rates and charge fees to pay for the costs of processing loans. The IFA is required to submit an annual report to the Governor and the General Assembly beginning October 1, 2018, detailing the expenditures of the previous year.
- 15.0% to the Division of Soil Conservation and Water Quality of the DALS for the Water Quality Urban Infrastructure Program to fund demonstration projects that decrease erosion and storm water discharge, and other related projects. The projects will be funded on a cost-share basis. The Division can use 4.0% of the funds for administration. Beginning July 1, 2019, funds can be used to support the three-year data collection of in-field practices at Iowa State University. Funds may also be used to develop and maintain a website displaying measurable indicators of change in State watersheds. Examples of measurable indicators include public and private funding inputs, land use, and calculated load reductions.

### **Background**

Currently, the sale of water by utilities to residential and nonresidential customers is subject to the State sales tax, as well as any local option sales tax (LOST). Nonresidential sewage utilities are also subject to the sales tax, while residential sewage utilities are not. The State sales tax includes a portion that is directed to the Secure an Advanced Vision for Education (SAVE) Program, commonly referred to as the “sixth-cent.”

The Wastewater Treatment Financial Assistance Program created in Iowa Code section [16.134](#) is for communities, with priority for disadvantaged communities, seeking to install or upgrade wastewater treatment facilities due to regulatory activity by the Department of Natural Resources (DNR). Grant awards are capped at \$500,000. The Fund received a total of \$11.0 million in appropriations from the Rebuild Iowa Infrastructure Fund (RIIF) for the period of FY 2006 to FY 2008.

### **Assumptions**

- The annual sales tax attributable to metered water sales in FY 2015 was estimated at \$20.3 million. This estimate was then increased by Moody’s projections of the Consumer Price Index (CPI) inflation index and population estimates from the REMI<sup>1</sup> forecast.
- Items or services exempt from the State sales tax are also exempt from any LOST. The Bill does not provide for a local option sales tax on water services.
- The Bill does not subject the new water service tax to the SAVE transfer.
- The section of the Bill related to the tax becomes effective July 1, 2018 (FY 2019), and the tax is repealed July 1, 2029.

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<sup>1</sup> REMI refers to Regional Economic Models, Inc. See <http://www.remi.com/> for more information.

- The Department of Revenue (DOR) will have administrative costs related to establishing the collection of the Water Service Excise Tax.
- The DNR will have increased expenditures for support and staff who provide technical assistance to the IFA for projects supported by the Wastewater and Drinking Water Financial Assistance Program.

### **Fiscal Impact**

#### **Water Quality Infrastructure Fund & Water Quality Financial Assistance Fund.**

The estimated flow of funds under current law and as proposed in SF 512 is shown in **Table 1**. General Fund revenue and SAVE dollars will be diverted to the Water Quality Financial Assistance Fund and the LOST revenues will no longer be collected.

<b>Table 1 - Current Law Sales Tax Policy vs. SF 512</b>									
(In Millions)									
	<b>Current Law</b>				<b>Senate File 512</b>				
	<b>Estimated Sales of Metered Water</b>	<b>General Fund</b>	<b>SAVE</b>	<b>LOST</b>	<b>General Fund</b>	<b>SAVE</b>	<b>LOST</b>	<b>Water Quality Infrastructure Fund</b>	<b>Water Quality Financial Assistance Fund</b>
FY 2019	\$ 386.5	\$ 19.3	\$ 3.9	\$ 3.4	\$ 19.3	\$ 0.0	\$ 0.0	\$ 1.9	\$ 1.9
FY 2020	398.1	19.9	4.0	3.5	15.9	0.0	0.0	4.0	4.0
FY 2021	408.7	20.4	4.1	3.6	12.3	0.0	0.0	0.0	12.3
FY 2022	419.4	21.0	4.2	3.7	12.6	0.0	0.0	0.0	12.6
FY 2023	431.1	21.6	4.3	3.8	12.9	0.0	0.0	0.0	12.9

Beginning in FY 2021, the Water Quality Infrastructure Fund will receive \$15.0 million per year from wagering tax receipts. The estimated fiscal impact is shown in **Table 2**.

<b>Table 2 - Net Impact of SF 512</b>						
(In Millions)						
	<b>General</b>			<b>Rebuild Iowa Infrastructure Fund</b>	<b>Water Quality Infrastructure Fund</b>	<b>Water Quality Financial Assistance Fund</b>
	<b>Fund</b>	<b>SAVE</b>	<b>LOST</b>	<b>Fund</b>	<b>Fund</b>	<b>Assistance Fund</b>
FY 2019	\$ 0.0	\$ -3.9	\$ -3.4	\$ 0.0	\$ 1.9	\$ 1.9
FY 2020	-4.0	-4.0	-3.5	0.0	4.0	4.0
FY 2021	-8.2	-4.1	-3.6	-15.0	15.0	12.3
FY 2022	-8.4	-4.2	-3.7	-15.0	15.0	12.6
FY 2023	-8.6	-4.3	-3.8	-15.0	15.0	12.9

Once the full transfer amount is reached in FY 2023, revenues will grow approximately 2.9% per year until the Program is repealed on July 1, 2029, or when the State sales tax is increased.

Moneys from the Water Quality Financial Assistance Fund will be appropriated as shown in **Table 3** and will continue through FY 2030.

**Table 3 - Appropriations from Water Quality Financial Assistance Fund**

<b>Fiscal Year</b>	<b>Wastewater and Drinking Water Treatment Financial Assistance Program</b>	<b>Water Quality Financing Program Fund</b>	<b>Water Quality Urban Infrastructure Fund</b>
FY 2018	\$ 855,000	\$ 760,000	\$ 285,000
FY 2019	\$ 1,800,000	\$ 1,600,000	\$ 600,000
FY 2020	\$ 5,535,000	\$ 4,920,000	\$ 1,845,000
FY 2021	\$ 5,670,000	\$ 5,040,000	\$ 1,890,000
FY 2022	\$ 5,805,000	\$ 5,160,000	\$ 1,935,000

**Other Expenditures.** The DOR estimates expenditures for implementing the Water Services Excise Tax at \$1.1 million for FY 2018. These include the following:

- \$800,000 for services from the Office of the Chief Information Officer.
- \$200,000 for services from First Data Government Services.
- \$58,000 for indirect expenditures by the DOR.

The DNR estimates an increase in expenditures for support and staff who provide technical assistance to the IFA for projects supported by the Wastewater and Drinking Water Financial Assistance Program. These expenditures are listed in **Table 4**. No funding source has been identified for these expenditures.

**Table 4 - Other Expenditures for SF 512**

	<b>FY 2018</b>	<b>FY 2019</b>	<b>FY 2020</b>	<b>FY 2021</b>	<b>FY 2022</b>	<b>Annual Expense FY 2023 - FY 2029</b>
DOR Expenditures	\$1,100,000	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0
DNR Expenditures	0	170,000	232,000	295,000	403,000	478,000
Total Other Expenditures	<u>\$1,100,000</u>	<u>\$170,000</u>	<u>\$232,000</u>	<u>\$295,000</u>	<u>\$403,000</u>	<u>\$478,000</u>
DNR FTE Positions		3.0	3.8	4.6	5.3	6.1

#### **Sources**

Department of Natural Resources  
Department of Revenue  
Iowa Finance Authority  
LSA calculations

/s/ Holly M. Lyons

April 18, 2017

The fiscal note for this Bill was prepared pursuant to Joint Rule 17 and the Iowa Code. Data used in developing this fiscal note is available from the Fiscal Services Division of the Legislative Services Agency upon request.